



U. S. Department of Justice

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To: All Chapter 7 Panel Trustees  
All Chapter 13 Standing Trustees

From: Carol A. Osborne, Regional Analyst 

Re: Handbook Changes/Check 21/Bank Statement and Canceled Check Requirements

The Executive Office has announced some upcoming changes to the *Handbook for Chapter 7 Trustees* that will impact audits starting in 2005. These changes stem primarily from the Check Clearing for the 21st Century Act, which goes into effect October 28, 2004, and the transition to ECF and paperless record keeping. The new law and the revised policies affect the trustees' procedures for maintaining cash receipts logs, bank reconciliations, supporting documentation for receipts and disbursements, case progress review and other related matters.

For example, these are some of the Check 21-Related changes:

- No more original canceled checks.
- Original canceled checks will still come in for awhile, but trustees will also see canceled checks as front and back images on bank stationery, 3 per page.
- The trustee's review of bank statements and canceled checks must be completed within 10 days of receiving the statements. Errors must be reported within 30 days of receiving statements.
- If the check images are illegible, the trustee needs to request a clearer image, a full-size image, or a substitute check (which is the legal equivalent to the original canceled check).

A revised Chapter 9 for the Handbook reflecting these and other related changes will be ready for distribution by the end of 2004. These changes will become effective January 1, 2005.

For chapter 7 trustees, for your reference attached is a summary of the talking points on New Chapter 7 Handbook Policies and a hand-out on bank reconciliations that were distributed at the NABT's San Diego conference. Regarding the final procedures to be implemented, we will keep you informed of the USTP's progress.

Attachments

## **Chapter 7 Trustee Bank Account Review and Reconciliation Procedures**

At the request of Chapter 7 Trustees and United States Trustee Program staff, this memorandum describes bank reconciliation procedures that meet current and pending Handbook requirements. Included are some additional procedures that can be accomplished simultaneously with the bank reconciliations.

### **Overview of Bank Reconciliations**

A bank reconciliation identifies the account balance per the bank statement and the account balance per the accounting records (Form 2), as of month end, and identifies the differences, such as deposits or transfers in transit, outstanding checks, NSF checks, service charges, and errors made by the bank or by the trustee. In general, deposits in transit and outstanding checks will resolve themselves without further action by the trustee (except for lost deposits, errors, or checks that have been outstanding for more than 90 days). Other reconciling items require the trustee to take specific action to correct the problem. For example, if a check is returned unpaid by the payer's bank, the trustee will need to record the NSF check on Form 2 and initiate collection proceedings.

### **Chapter 7 Trustee Bank Account Review and Reconciliation Procedures**

1. Core bank account review and reconciliation requirements:
  - a. Monthly review and reconciliation of all bank accounts;
  - b. Timely posting of all banking transactions on Form 2 (except for bank errors that are reversed in the same month);
  - c. Timely investigation of unusual items;
  - d. Timely follow up of reconciling items that require correction; and
  - e. Trustee supervision of, and involvement with, the reconciliation process.
2. Trustee review of bank statements and canceled checks for unusual items (Handbook p. 9-16, Section D.1.b):
  - a. The person who receives the mail gives the unopened envelopes containing the monthly statements and canceled checks directly to the trustee.
  - b. The trustee reviews the statements and canceled checks for errors, unusual transfers and endorsements, alterations, and forged or unauthorized signatures within ten days of receipt (and before giving the documents to an assistant to prepare the bank reconciliations).
  - c. If discrepancies are discovered, the trustee brings them to the bank's attention immediately (e.g., within ten days of receiving the bank statements).
  - d. With Check 21, the canceled checks may be front and back check images printed on paper. If any canceled check image is illegible, the trustee requests a clearer image, a full-size image, or a substitute check.
  - e. The trustee is not required to initial and date the bank statements as evidence of this review.

3. Comparison of bank statement and Form 2 balances (Handbook page 9-16, Section 2, et. al.)

- a. On a monthly basis, the trustee or an assistant reconciles all bankruptcy estate accounts before the end of the following month.
- b. The reconciliation can be documented on the face of the bank statement or another form created for this purpose. A bank reconciliation report printed from the trustee's case management system may be used. A complete reconciliation contains the following information:

- (1) Bank statement balance
- (2) Form 2 balance
- (3) All reconciling items, individually identified and explained (see d below)
- (4) Preparer's initials and the date to document who prepared the reconciliation
- (5) Trustee's initials and the date for a sample of reconciliations selected by the trustee to review and approve

Note: Initials and dates on the bank statements, by themselves, do not constitute a bank reconciliation. The preparer must record the Form 2 balance on the statement, note the difference, and explain the reconciling items if the difference is other than zero.

- c. If the trustee uses reports generated by the case management system, the following additional procedures apply:
  - (1) The report, usually a summary of all open bank accounts in one report, must have a cut-off date that matches the bank statement date (e.g., end of the calendar month).
  - (2) Both the bank statement balance and the Form 2 balance for each account must appear on the report.
  - (3) Each bank statement balance must be compared with the balance on the physical bank statement to verify that they match. This comparison may be documented with check marks. Note: it is necessary to validate the bank statement balances per the system-generated report against the physical bank statements to ensure that the report is accurate.
  - (4) If the bank statement balance and Form 2 balance do not match, a detail reconciliation must be prepared or printed so that the differences can be itemized and investigated (see d. below).
  - (5) Both the preparer and the trustee (if not the preparer) must initial and date the report to document who prepared and who reviewed and approved the reconciliation.

- (6) Reconciliation reports containing multiple accounts should be kept in chronological order in a file or notebook. Reconciliation reports for individual accounts should be kept with the bank statements in the estate files.

d. Disposition of reconciling items:

- (1) If the difference is due to a deposit or transfer in transit, the amount is matched to the latest deposit/transfer on Form 2. This deposit or transfer should have been made within 1 - 2 days of month end. If an older deposit or transfer is still in transit, the trustee needs to investigate the reason. The deposit could have been posted to the wrong account in the trustee's system or lost in transit to the bank. A delayed transfer could be due to bank error.
- (2) If the difference is due to outstanding checks, the dates and amounts of the checks are verified against Form 2. If any checks are more than 90 days old, the trustee needs to determine why the checks have not cleared, void them on Form 2, issue stop payments, and re-issue the checks.
- (3) If the difference is due to a service charge or back up withholding, the trustee needs to contact the bank to reverse the charges and record the item on Form 2.
- (4) If the difference is due to an NSF check, the trustee needs to contact the payer to replace the check. The item is recorded on Form 2 and formally tracked in an NSF check log.
- (5) If any reconciling item is due to bank error, it should be brought to the bank's attention within 30 days of receiving the bank statements.

4. As the bank reconciliations are being prepared, it is a good time to do the following:

- a. If an account has a zero balance and the TDR has been filed, the trustee should arrange with the bank to close the account.
- b. The trustee or assistant should verify that all canceled checks listed on the bank statement have been received. This will save time later when gathering the bank records to submit to the United States Trustee with the TFR. This also enables the trustee or assistant to identify checks that cleared the bank without a check number (due to bank error).
- c. The trustee or assistant can verify that estate funds are properly invested.
- d. The trustee can verify, on a test basis, that incoming receipts are promptly and properly deposited by comparing the cash receipts log to the deposit slips and bank statements.

**NABT San Diego**  
**Audit and Field Exam Presentation**  
**Talking Points on New Chapter 7 Handbook Policies**  
**Effective 1/1/05 (except for Check 21-Related Changes)**

**Cash Receipts Log**

- The format and requirements for the cash receipts log are being modified to enable the log to be kept electronically. Also, we have determined that some features have not proven necessary.
- The date deposited column is no longer required. Access to the log should be limited to the trustee and the person who opens the mail. The person who prepares and makes the deposit and posts entries to Form 2 should not have access to the log (unless the Trustee does everything). If the trustee has only one assistant, the trustee should consider being the person who maintains the log.
- The purpose column is now a multi-purpose column, called “remarks.” For a electronic cash receipts log, the trustee can electronically record his or her testing of sample receipts by making a notation of the date and deposit amount in this column. For handwritten logs, the sampled receipts should continue to be initialed and dated by the trustee.

**Bank Reconciliations**

- Some of the bank reconciliation requirements are being modified to:
  - ✓ Ease the burden on trustees
  - ✓ Clarify what is required to be kept in paper form
  - ✓ Define required time frames
- The trustee may review, initial, and date individual bank account reconciliations (defined below) on a sample basis.
- The trustee no longer needs to initial and date every bank statement.
- The format for bank reconciliations will be provided as a handout, at the request of Chapter 7 Trustees and UST staff. The significant provisions are:
  - ✓ The trustee must review the bank statements and canceled checks within ten days of receiving the bank statements.
  - ✓ Bank reconciliations must be completed before the end of the following month.
  - ✓ Errors need to be reported to the bank within 30 days of receiving the bank statement.
  - ✓ Bank reconciliations may be documented on the face or the back of each bank statement, showing the bank balance, Form 2 balance, and each reconciling item.

- ✓ The bank reconciliation summary report from the trustee's system may be used for all accounts where bank balance = Form 2 balance. Both the trustee and preparer initial and date the summary.
- ✓ Individual account reconciliations must be prepared (or generated from the trustee's computer system) for accounts that are out of balance. The preparer must initial and date each individual account reconciliation. The trustee must review the reconciliations at least on a sample basis, initialing and dating only those that are reviewed.
- ✓ It is not sufficient to view the bank reconciliation on the computer screen, as this procedure does not provide an audit trail. Proper bank reconciliations are handwritten or printed from the trustee's system. Essentially, this is the only item that must be kept in paper form in a paperless environment (except for bank statements and canceled checks and the other exclusions mentioned in the Handbook).

### **Supporting documentation for receipts and disbursements**

- A "paid" stamp or check copy to prevent duplicate payments is no longer necessary, as duplicate payments are rare.
- The requirements for supporting documentation for receipts and disbursements are being clarified:
  - ✓ Supporting documentation for receipts, such as copies of checks and transmittal letters, must be kept in the estate file. Sale orders or notices and reports of sale must also be kept in the estate file if not available electronically from the court or if they contain other information that supports the receipt, such as the trustee's handwritten notations about the sale. Supporting documentation should contain the related docket entry or date, when applicable.
  - ✓ Supporting documentation for disbursements, such as invoices and fee applications, should indicate the trustee's review and approval and be kept in the estate file. Court orders for disbursements (when required) must also be kept in the estate file if not available electronically from the court or if the amount on the invoice or fee application differs from the amount approved in the court order. The supporting documentation should contain the date or docket entry for the court order, the check number, and the date paid. If there is no supporting documentation other than a court order, a copy of the check may serve as supporting documentation.

### **Case Progress Review**

- The requirements for the case progress review are being modified to enable the review to be conducted and documented electronically.
- Evidence of the case progress review may be kept electronically or in paper form. This documentation should reflect the date of the trustee's review but does not need to be initialed. Hence, no need to print the notes in order to record the trustee's initials.
- The trustee may review individual cases on a rotating basis, as long as each case is reviewed at least quarterly.
- The trustee's records must indicate regular and ongoing management of the cases.

### **Check 21-Related Changes**

- No more original canceled checks.
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### **Changes Related to ECF and Paperless Not Mentioned Elsewhere**

- Court fees, such as filing fees for adversary proceedings, may be paid electronically using the trustee's personal or firm credit card. Absent local rules or practices to the contrary, the trustee may be reimbursed with an estate check.
- Unclaimed funds (e.g., payments to creditors that do not clear the bank) must be paid to the court using an estate check. Electronic payment is not permitted.
- The receivables ledger may be kept electronically.
- ECF passwords need to be protected just like case management system password. The both need to be changed annually and when an employee is terminated or no longer needs access.

## **Audit Changes for 2005**

- Testing will be streamlined and focus on the more important aspects of the trustee operation. For example:
  1. Auditors will be verifying that bank accounts reconcile, not focusing on initials and dates.
  2. Auditors will be verifying that disbursements are authorized and that check amounts match the authorizing and supporting documents, not looking for a paid stamp (which is being eliminated as a Handbook requirement).
  3. Tests of information on Forms 1 and 2 will be modified to focus on the most important areas, such as whether Form 1 contains all assets, correctly reflects liquidations and abandonments, and accurately describes the case's current status per the trustee's records.
  4. Tests of the trustee's case progress review procedures will focus on evidence of activity in the case or notations in the case file on a quarterly basis, rather than on whether the trustee has initialed and dated the file or other case progress review documentation.
- *De minimis* findings such as "incorrect bond amount on Form 3" and "no 'u' for unscheduled assets on Form 1" will no longer be reported.
- The audit focus will shift from transactions to assets, although transactions will still be tested.
- Fifteen cases will be selected for testing, including cases without funds.
- If the trustee maintains a "paperless" filing system, the trustee should be prepared to download to CD-Rom the estate files and records for cases selected by the auditor, examiner, or reviewer. The trustee also may be asked to print documents from the trustee's case management system or the court file.